Nos. 90-1361, 90-1484 (9) (10)

In The

Supreme Court of the United States

October Term, 1991

HOLYWELL CORPORATION, *et al.*,

Petitioners,

v.

FRED STANTON SMITH, *et al.*,

Respondents.

UNITED STATES OF AMERICA,

Petitioner,

v.

FRED STANTON SMITH, *et al.*,

Respondents.

On Writs Of Certiorari To The United States Court Of Appeals For The Eleventh Circuit

BRIEF OF CALIFORNIA, CONNECTICUT, DELAWARE, DISTRICT OF COLUMBIA, FLORIDA, GEORGIA, HAWAII, ILLINOIS, INDIANA, IOWA, KANSAS, LOUISIANA, MAINE, MARYLAND, MASSACHUSETTS, MICHIGAN, MINNESOTA, MISSISSIPPI, MISSOURI, MONTANA, NEW JERSEY, NEW MEXICO, NEW YORK, NORTH DAKOTA, OREGON, PENNSYLVANIA, RHODE ISLAND, SOUTH CAROLINA, TENNESSEE, TEXAS, UTAH, VIRGINIA, WEST VIRGINIA AND THE CITY OF NEW YORK AS AMICI CURIAE IN SUPPORT OF PETITIONERS

MARY SUE TERRY
Attorney General of Virginia

H. LANE KNEEDLER
Chief Deputy
Attorney General

K. MARSHALL COOK
Deputy Attorney General

BARBARA M. ROSE
Senior Assistant
Attorney General

MARTHA B. BRISSETTE*
JOHN PATRICK GRIFFIN
Assistant Attorneys General

Office of the Attorney General
101 N. Eighth Street
Richmond, Virginia 23219
(804) 786-0061

*Counsel of Record for Amici Curiae

(Counsel Continued on Inside Cover)

COCKLE LAW BRIEF PRINTING CO., (800) 225-6964
OR CALL COLLECT (402) 342-2831

34

DANIEL E. LUNGREN
Attorney General of California

RICHARD BLUMENTHAL
Attorney General of Connecticut

CHARLES M. OBERLY, III
Attorney General of Delaware

JOHN PAYTON
Corporation Counsel for the
District of Columbia

ROBERT A. BUTTERWORTH
Attorney General of Florida

MICHAEL J. BOWERS
Attorney General of Georgia

WARREN PRICE, III
Attorney General of Hawaii

ROLAND W. BURRIS
Attorney General of Illinois

LINLEY E. PEARSON
Attorney General of Indiana

BONNIE J. CAMPBELL
Attorney General of Iowa

ROBERT T. STEPHAN
Attorney General of Kansas

WILLIAM J. GUSTE, JR.
Attorney General of Louisiana

MICHAEL E. CARPENTER
Attorney General of Maine

J. JOSEPH CURRAN, JR.
Attorney General of Maryland

SCOTT HARSHBARGER
Attorney General of Massachusetts

FRANK J. KELLEY
Attorney General of Michigan

HUBERT H. HUMPHREY, III
Attorney General of Minnesota

Michael C. Moore
Attorney General of Mississippi

William L. Webster
Attorney General of Missouri

Marc Racicot
Attorney General of Montana

Robert J. Del Tufo
Attorney General of New Jersey

Tom Udall
Attorney General of New Mexico

Robert Abrams
Attorney General of New York State

Nicholas J. Spaeth
Attorney General of North Dakota

Dave Frohnmayer
Attorney General of Oregon

Ernest D. Preate, Jr.
Attorney General of Pennsylvania

James E. O'Neil
Attorney General of Rhode Island

T. Travis Medlock
Attorney General of South Carolina

Charles W. Burson
Attorney General and Reporter of Tennessee

Dan Morales
Attorney General of Texas

R. Paul Van Dam
Attorney General of Utah

Mario J. Palumbo
Attorney General of West Virginia

Victor A. Kovner
Corporation Counsel for the City of New York

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page

TABLE OF AUTHORITIES – Continued

Page

TABLE OF AUTHORITIES – Continued

TABLE OF AUTHORITIES – Continued

TABLE OF AUTHORITIES – Continued

TABLE OF AUTHORITIES – Continued

Nos. 90-1361, 90-1484

In The

Supreme Court of the United States

October Term, 1991

HOLYWELL CORPORATION, *et al.*,

Petitioners,

v.

FRED STANTON SMITH, *et al.*,

Respondents.

UNITED STATES OF AMERICA,

Petitioner,

v.

FRED STANTON SMITH, *et al.*,

Respondents.

On Writs Of Certiorari To The United States Court Of Appeals For The Eleventh Circuit

BRIEF OF CALIFORNIA, CONNECTICUT, DELAWARE, DISTRICT OF COLUMBIA, FLORIDA, GEORGIA, HAWAII, ILLINOIS, INDIANA, IOWA, KANSAS, LOUISIANA, MAINE, MARYLAND, MASSACHUSETTS, MICHIGAN, MINNESOTA, MISSISSIPPI, MISSOURI, MONTANA, NEW JERSEY, NEW MEXICO, NEW YORK, NORTH DAKOTA, OREGON, PENNSYLVANIA, RHODE ISLAND, SOUTH CAROLINA, TENNESSEE, TEXAS, UTAH, VIRGINIA, WEST VIRGINIA AND THE CITY OF NEW YORK AS AMICI CURIAE IN SUPPORT OF PETITIONERS

INTRODUCTORY STATEMENT

Pursuant to United States Supreme Court Rule 37.2, the signatory States, the District of Columbia and the City of New York submit this Brief as Amici Curiae supporting Petitioners to apprise the Court of significant nonfederal governmental interests implicated by the decision of the United States Court of Appeals for the Eleventh Circuit ("court of appeals") in this case. Because this Brief is sponsored and filed by the aforementioned governments, consent to its filing is not required. U.S. Sup. Ct. R. 37.5.

INTEREST OF THE AMICI CURIAE

The States, as sovereigns that must function effectively in our federal system, have a vital interest in the collection of taxes in the bankruptcy process. No nonfederal officer or agency is a party to this case because the trustee (Fred Stanton Smith) failed to include any as parties to his declaratory judgment action against the United States and the debtors.[1] The court of appeals'

[1] As a result, the court of appeals focused exclusively on the federal income tax issue. However, the trustee has not paid state income taxes either, and an affirmance by the Court will threaten the public fisc of the States, as well as the federal government. A trustee who considers himself free of the obligation to pay federal income taxes cannot be expected to honor his obligations to pay state income taxes. In the case of Holywell Corporation, the Virginia Department of Taxation in March 1988 conducted a field audit for the fiscal year ending July 31, 1986, during which Miami Center was sold, and assessed corporate income tax, penalties, and interest totaling

(Continued on following page)

decision in the case sanctions a new tax-avoidance device that could adversely affect States' ability to collect taxes in bankruptcy cases. Instead of a regular "trustee" subject to all state and local taxes (*California State Bd. of Equalization v. Sierra Summit, Inc.*, 490 U.S. 844, 853 (1989)), bankruptcy participants can now agree on a standard-form "reorganization plan" calling for a "liquidating trustee" to liquidate the bankruptcy estate and thereby avoid all state and local (as well as federal) taxes incurred during the liquidation process.

The taxing power is "one of the primary indicia of sovereignty," *Illinois v. Kentucky*, 111 S.Ct. 1877, 1882 (1991), and this Court "has recognized repeatedly that state sovereignty is a fundamental component of our system of government." *Garcia v. San Antonio Metropolitan Transit Authority*, 469 U.S. 528, 573 (1985) (Powell, J. dissenting). Indeed, as this Court stated more than a century ago, "[i]t is upon taxation that the several States chiefly rely to obtain the means to carry on their respective

(Continued from previous page)

over $1.3 million. The trustee, through his attorney, Mr. Herbert Stettin, has refused to pay the assessment.

For the fiscal year ending July 31, 1985, the debtor Holywell Corporation through its President Theodore B. Gould in February 1988 filed a Virginia state income tax return reporting capital gains from the preconfirmation sale of properties in the Washington, D.C. area, with a letter demanding payment of the tax liability from the Miami Center Liquidating Trust. The Virginia Department of Taxation made certain adjustments to the return as filed and in March 1988 assessed corporate income tax, penalty and interest totaling $147,418. The trustee has also refused to pay this assessment.

governments." *Dows v. City of Chicago*, 78 U.S. (11 Wall.) 108, 110 (1871). It is, therefore, "the imperative duty of the court to recognize as paramount, and enforce with promptness and vigor, the just claims of the authorities for the prescribed contributions to state and municipal revenue. . . . The courts of the United States have always recognized the importance of leaving the powers of the State[s] in respect to taxation unimpaired." *In re Tyler*, 149 U.S. 164, 187 (1893).

The signatory Amici believe that the court of appeals' decision overlooks an important federal statute, 28 U.S.C. § 960, that clearly requires all fiduciaries acting under the authority of a federal court, including the so-called "contract trustee" in this case, to report and pay applicable state and local taxes incurred in the liquidation process. This statute provides:

> Any officers and agents conducting any business under authority of a United States court shall be subject to all Federal, State and local taxes applicable to such business to the same extent as if it were conducted by an individual or corporation.

28 U.S.C. § 960.[2]

---

[2] The plain language of 28 U.S.C. § 960, which applies to "*[a]ny* officers and agents conducting *any* business under authority of a United States court" (emphasis added), is broader than § 6012(b)(3) of the Internal Revenue Code (26 U.S.C.), which applies to "a receiver, trustee in a case under title 11 of the United States Code, or assignee" having possession of or title to all or substantially all of a corporation's

(Continued on following page)

SUMMARY OF ARGUMENT

The decision below creates a dangerous loophole that—if sustained—could enable private creditors to avoid state and local as well as federal taxes through a technicality that violates the plain meaning and purpose of 28 U.S.C. § 960, as well as the structure of the Bankruptcy Code and parallel state statutes. The court of appeals ruled that a trustee of a trust created to liquidate a corporation's assets as part of a Chapter 11 bankruptcy reorganization plan need not report and pay federal (and thus by implication state) income taxes on either capital gains resulting from the liquidation process or income earned by the trust. In this case, the trustee's failure to file returns or pay state income taxes has created a liability to the Commonwealth of Virginia exceeding one million dollars.

Although the court of appeals did not address it, a federal statute (28 U.S.C. § 960) quite clearly requires the payment of state as well as federal and local taxes, as this Court has confirmed on several occasions. The court of appeals' failure to acknowledge the applicability of § 960 could by implication negate the trustee's obligation to report and pay state taxes, regardless of the provisions of state law.

(Continued from previous page)

property. The signatory Amici maintain that § 960, which was cited to the court of appeals by the debtors, requires the trustee in this case to pay applicable state and local taxes regardless of whether the court of appeals was correct in its interpretation of § 6012(b)(3) of the Internal Revenue Code.

In adopting § 960, Congress meant to preserve States' ability to collect taxes, an essential attribute of sovereignty vital to States' ability to function effectively within our federal system. This Court recently examined the language, legislative history and jurisprudence of § 960 and concluded that the statute requires any officer or agent appointed by a United States court, including a bankruptcy trustee, to pay state taxes "on the liquidation process." *California State Bd. of Equalization v. Sierra Summit, Inc.*, 490 U.S. 844, 853 (1989). The Court added, " 'Congress has, in the interest of justice or good will, by this Act directed the trustee to pay rather than litigate these tax claims. By the sweeping terms of this statute all doubts have been resolved in favor of the state taxes.' " 490 U.S. at 852-53 n.9 (quoting *Thompson v. Louisiana*, 98 F.2d 108, 111 (8th Cir. 1938)). Other decisions have recognized the "plain language" Congress used to require a broad spectrum of court officers to pay state and local taxes.

A trustee's duties under § 960 to report and pay state and local taxes affirm duties imposed by the Bankruptcy Code and parallel state statutes. The Bankruptcy Code ordinarily requires the trustee (or debtor-in-possession) to file state and local tax returns and to pay applicable state and local taxes. 11 U.S.C. §§ 346(c)(2), 728(b), 1146(b). In addition, state and local taxes incurred on sales during the course of the bankruptcy are treated as administrative expenses. 11 U.S.C. §§ 503(b)(1)(B)(i), 507(a)(1). Parallel state statutes also require trustees of bankrupt corporations to report and pay state taxes, an obligation Congress expressly recognized and preserved in enacting 28 U.S.C. § 960.

The court of appeals' decision imposes an undue administrative burden on state and local governments. Because corporations and other business organizations often operate in multiple jurisdictions, many bankruptcy cases result in tax liabilities to numerous States and localities. These States and localities are unlikely to be listed on the debtor's schedule of liabilities or to have any notice of a potential threat to their revenues. That is particularly true when, as here, taxes are incurred *after* the plan has been confirmed.

State and local governments cannot realistically be expected to track every bankruptcy case in every federal district in the nation to watch for the establishment of liquidating trusts and the confirmation of reorganization plans that fail to provide for payment of state and local taxes incurred after confirmation. In enacting 28 U.S.C. § 960, Congress chose to require all federally appointed fiduciaries acting under the authority of United States courts, including the bankruptcy courts, to assume the obligation of voluntarily reporting and paying applicable state and local taxes.

ARGUMENT

I. Introduction

The bankruptcy court in this case approved a liquidation of the debtors' assets. Rather than use the ordinary bankruptcy process of Chapter 7 liquidation or have a bankruptcy trustee or the debtors-in-possession liquidate in the Chapter 11 proceeding, however, the court agreed with the debtors' major creditor (the Bank of New York)

that a "liquidating trust" should be created as part of a "plan of reorganization." The court of appeals held, in a split decision, that the trustee of this liquidating trust was not required to report and pay federal (and thus by implication state) income taxes on capital gains and interest realized through the liquidation process, because he was "not a trustee under Title 11, but rather a contract trustee performing essentially limited and ministerial duties." Pet. App. 11a; 911 F.2d at 1545.[3] Instead, the debtors—whose assets were transferred to the trustee's control as part of the Bank's "reorganization" plan—are apparently supposed to pay the taxes. In the case of the Holywell Corporation (which had the bulk of the tax liability), this cynically leaves a corporate shell with no assets—and the state and federal treasuries—holding the bag.[4] Such a result contravenes the Bankruptcy Code's basic goal of providing the reorganized debtor a fresh start through payments made in accordance with an orderly statutory scheme establishing the rights and priorities of competing creditors, including federal, state and local tax collectors. *See* 11 U.S.C. § 506 (rights of secured creditors); 11 U.S.C. § 507 (schedule of priorities among unsecured creditors).

---

[3] As the Solicitor General has observed, the term "contract trustee" appears to have no basis in federal jurisprudence.

[4] As noted, for the fiscal year ending July 31, 1985, the debtor Holywell Corporation filed a Virginia state income tax return reporting gains from the preconfirmation sale of the Washington properties, but has made no payment of the outstanding state tax liability for that year. For the fiscal year ending July 31, 1986, there has been neither a state income tax

(Continued on following page)

The signatory Amici request this Court to reverse the court of appeals' decision for three reasons. First, it ignores § 960 of the Judicial Code, through which Congress chose to protect an essential building block of federalism by requiring any fiduciary acting under the authority of a federal court to comply with state and local tax laws. Second, the court of appeals' decision is inconsistent with the structure of the Bankruptcy Code and parallel state statutes. Finally, it imposes an undue administrative burden on state and local government officials to monitor and enforce trustees' compliance with state and local tax laws on a nationwide basis.

II. 28 U.S.C. § 960 Is a Clear Congressional Mandate Requiring All Federally Appointed Fiduciaries to Report and Pay Federal, State and Local Taxes

The court of appeals clearly overlooked § 960 of the Judicial Code. This statute plainly requires any fiduciary acting under the authority of a federal court, including this trustee, to file returns and pay applicable federal, state and local taxes:

> Any officers and agents conducting any business under authority of a United States court shall be subject to all Federal, State and local taxes applicable to such business to the

---

(Continued from previous page)

return, nor any payment. State law has likewise been ignored with respect to continuing postconfirmation earnings.

same extent as if it were conducted by an individual or corporation.

28 U.S.C. § 960. The statute subjects the trustee's business activities to state and local (as well as federal) taxes "to the same extent" as if they were conducted by an individual or corporation. The "plain meaning" of the phrase "conducting any business" includes liquidating a business or the estate of an entity conducting a business. *See California State Bd. of Equalization v. Sierra Summit, Inc.*, 490 U.S. 844, 851 (1989).

Section 960 is a specific articulation of a federally appointed fiduciary's general statutory obligation under 28 U.S.C. § 959(b) to manage and operate the debtor's property according to applicable state law requirements. *See Kansas City v. Johnson*, 70 F.2d 360 (8th Cir.), *cert. denied*, 293 U.S. 617 (1934) (federal receiver not exempt from state and local taxes under predecessor statute).[5]

As Chief Justice Rehnquist has stated, § 960 is "plain on its face" and embodies Congress' "express mandate" that the payment of state taxes is "[t]he paramount federal interest" to which federal courts must defer in bankruptcy cases. *New Jersey v. Reading Co.*, 451 U.S. 918, 918-20 (1981) (Rehnquist, J., dissenting from denial of certiorari). This "express mandate" reflects Congress' choice to promote our system of federalism—a "unique

[5] Present § 959 is based on former 28 U.S.C. §§ 124 and 125 as enacted by Act of March 3, 1911, ch. 231, §§ 65, 66, 36 Stat. 1087, 1104-05, which preceded the 1934 enactment of a specific rule for taxes in § 960. *See* Act of June 18, 1934, ch. 585, 48 Stat. 993.

feature of the United States . . . guaranteed by the Constitution and implicit in the very name of our country." *Garcia v. San Antonio Metropolitan Transit Authority*, 469 U.S. 528, 560 (1985) (Powell, J., dissenting).[6]

The court of appeals' failure to acknowledge the clear applicability of 28 U.S.C. § 960 also impliedly negates parallel state statutes explicitly requiring trustees of corporations in bankruptcy to file returns reporting income arising out of the liquidation process.[7] Such implied

[6] *Accord Gregory v. Ashcroft*, 59 U.S.L.W. 4714, 4716 (U.S. Sup. Ct. June 20, 1991) (" 'the preservation of the States, and the maintenance of their governments, are as much within the design and care of the Constitution as the preservation of the Union and the maintenance of the National government.' " (quoting *Texas v. White*, 74 U.S. (7 Wall.) 700, 725 (1869)).

[7] *See, e.g.*, Va. Code Ann. § 58.1-441 (1991), which provides in pertinent part:

> Receivers, trustees in dissolution, trustees in bankruptcy, and assignees, operating the property or business of corporations must make returns of income for such corporations. If a receiver has full custody of and control over the business or property of a corporation, he shall be deemed to be operating such business or property, whether he is engaged in carrying on the business for which the corporation was organized or only in marshaling, selling, or disposing of its assets for purposes of liquidation.

See also, e.g., Cal. Rev. & Tax Code §§ 6005, 6019 (1987) (sales and use tax) 17004, 17006, 17007 (1983) (personal income tax), 23038, 23039, 25403 (1979 & Supp. 1991) (bank and corporation tax); D.C. Code Ann. § 47-1808.1 (1990); Fla. Stat. Ann. §§ 214.52, 220.11 (West 1989); 1991 Haw. Sess. Laws, Act 23 (amending Haw. Rev. Stat. § 237-1 (1985)); Ind. Code Ann. § 6-2.1-5-7 (Burns 1989); Kan. Stat. Ann. § 79-3220(b) (1989); La. Rev. Stat. Ann. § 47:2102 (West 1990); Md. Tax—Gen. Code

(Continued on following page)

preemption of state law requirements cannot be sustained in light of Congress' plainly expressed intent in 28 U.S.C. § 960 to protect States' sovereign power of taxation by requiring fiduciaries acting under the authority of a federal court to comply with state law requirements.

As noted previously, the power to lay and collect taxes is a fundamental attribute of state sovereignty, a power critical to States' ability to function effectively in our federal system. The plain language of the federal statute requires any federally appointed fiduciary to consult and comply with applicable state and local tax laws.[8]

This Court's decisions confirm that the plain language of 28 U.S.C. § 960 applies generally to taxation of all activities of all officers operating businesses under federal court authority, without exception. The Court first applied the statute in 1939. Writing for a unanimous Court, Justice Black—who, as a member of the Senate,

(Continued from previous page)

Ann. §§ 10-804, 1-101(p) (1988); Minn. Stat. Ann. § 289A.08, Subd. 2 (Supp. 1991); Mo. Ann. Stat. §§ 143.481, 143.501 (Vernon 1976) (income tax), 144.010(5) & (9), 144.021 (Vernon Supp. 1991) (sales and use taxes); N.Y. City Admin. Code §§ 11-603(3) (1966), 11-1701 (1986); N.Y. Tax Law § 601(c) & (e) (McKinney 1987 & Supp. 1991); R.I. Gen. Laws § 44-11-36 (1988); Tenn. Admin. Comp. § 1320-5-1-.57 (1991); Tex. Tax Code Ann. §§ 151.008(b)(2), 151.052 (Vernon 1982 & Supp. 1991); Utah Code Ann. § 59-7-143 (1987).

[8] Under § 960, the state tax laws with which trustees must comply include income and sales and use taxes. Forty-four States and the District of Columbia impose a corporate income tax, forty-two States impose a tax on at least some forms of personal income, and Michigan imposes a "Single Business Tax" on corporations and individuals. Forty-four States impose sales and use taxes. *See* J. Hellerstein, *State Taxation: I Corporate Income & Franchise Taxes* ¶ 1.6, at 20-23 (1983).

was present when the Act was considered and passed in 1934[9]—recognized the statute's broad applicability:

> Congress has here with vigor and clarity declared that a trustee and other court appointees who operate businesses must do so subject to state taxes "the same as if such business[es] were conducted by an individual or corporation."
>
> *   *   *
>
> The Act of 1934 indicates a Congressional purpose to facilitate—not to obstruct—enforcement of state laws; the court below correctly recognized and applied this Congressional purpose . . . [by holding a bankruptcy trustee liable for California taxes and penalties for his failure to pay them].

Boteler v. Ingels, 308 U.S. 57, 61 (1939).

This Court recently considered at length the applicability of § 960 to trustees appointed by bankruptcy courts. *See California State Bd. of Equalization v. Sierra Summit, Inc.*, 490 U.S. 844 (1989) ("*Sierra Summit*"). In *Sierra Summit*, the respondent relied on § 960 to argue that the imposition of California sales and use taxes on a bankruptcy liquidation sale impermissibly encroached on the federal bankruptcy process. The Court examined the statute and the bankruptcy laws and concluded that "[n]othing in the plain language of the statute, its legislative history, or the structure of the Bankruptcy Code indicates that Congress intended to exclude taxes on the liquidation process from those taxes the States may impose on the bankrupt estate." 490 U.S. at 853.

[9] 78 Cong. Rec. 11,466 (1934).

Section 960, of course, applies to all state and local taxes, including income taxes—as well as federal taxes. "Read most naturally, the statute evinces an intention that a State be permitted to tax a bankruptcy estate . . . and that, as a matter of federal law, 'a business in receivership, or conducted under court order, should be subject to the same tax liability as the owner would have been if in possession and operating the enterprise.' " *Sierra Summit*, 490 U.S. at 852 (quoting *Palmer v. Webster & Atlas Nat'l Bank of Boston*, 312 U.S. 156, 163 (1941)). As the *Sierra Summit* Court explained, " '[b]y the sweeping terms of this statute all doubts have been resolved in favor of the state taxes.' " 490 U.S. at 852-53 n.9 (quoting *Thompson v. Louisiana*, 98 F.2d 108, 111 (8th Cir. 1938)).

The legislative history also confirms Congress' sweeping intent—consistent with the structure of the Constitution and the federalism concept embodied in the Tenth Amendment—to preserve state tax collection authority in the bankruptcy liquidation context. Indeed, the committee reports reflect a congressional intent to supersede a federal district court ruling that under the common law, property in the hands of a receiver is not subject to tax.[10] "No good reason is perceived why a receiver should be permitted to operate under such an advantage as against his competitors not in receivership, and the States and local governments be deprived of this revenue." H.R. Rep. No. 1138, 73d Cong., 2d Sess. 1 (1934); S. Rep. No. 1372, 73d Cong., 2d Sess. 1 (1934).

---

[10] *Howe v. Atlantic, Pac. & Gulf Oil Co.*, 4 F. Supp. 162, 163-64 (W.D. Mo. 1933), *rev'd on state law grounds sub nom. Kansas City v. Johnson*, 70 F.2d 360, 361 (8th Cir.), *cert. denied*, 293 U.S. 617 (1934).

The bill was amended on the House floor without debate to apply not only to receivers but also to a "liquidator, referee, trustee, or other officer or agent." 78 Cong. Rec. 6,656 (1934). When Congress revised the Judicial Code in 1948, it deleted most of this enumeration as redundant, leaving only the present-day "any officers and agents" subject to state and local taxes. H.R. Rep. No. 308, 80th Cong., 1st Sess. 5, A102-03 (1948). *See also* W. Plumb, *The Tax Recommendations of the Commission on the Bankruptcy Laws—Income Tax Liabilities of the Estate and the Debtor*, 72 Mich. L. Rev. 935, 940 (1974). Congress' clear intent was that the phrase "any officers and agents" encompass a broad range of court-appointed individuals, including—specifically—a "liquidator" or a "trustee."

There can be no doubt that the phrase "officer[ ] and agent[ ] conducting any business under authority of a United States court" fits this trustee like a glove. His authority to conduct liquidating processes with respect to the debtors' business was derived from the order of the bankruptcy court approving the Plan of Reorganization; he filed a fidelity bond in favor of the United States with the court; and the bankruptcy court retained jurisdiction "to make any orders which may be necessary or appropriate to carry out the provisions of [the] Plan" until the trustee had made all "payments and distributions called for under the Plan." Pet. App. 46a.

III. 28 U.S.C. § 960 Affirms Duties Imposed by The Bankruptcy Code and Applicable State Laws

The intent expressed in § 960 harmonizes with duties imposed on trustees by the Bankruptcy Code and applicable

state law. Various provisions of the Bankruptcy Code confirm Congress' intent that the trustee in a bankruptcy case assume the debtors' obligations to report and pay all accruing taxes, state, local and federal. *See* W. Plumb, 72 Mich. L. Rev., *supra*, at 940. Three separate sections of the Bankruptcy Code require the trustee to file the appropriate state and local tax returns for various types of debtors.[11] Section 505(b) of the Bankruptcy Code further provides the trustee a procedure (initiated by filing a return) for obtaining an expedited determination of any tax liability incurred during the administration of the estate. And it is the *estate*, not the emerging debtor, that is generally responsible for the payment of taxes incurred in the administration of the estate.[12] As the Senate Judiciary Committee explained,

[11] 11 U.S.C. § 346(c)(2) (trustee of corporation or partnership); 11 U.S.C. § 728(b) (trustee for individual or corporation in Chapter 7 where debtor has net taxable income for entire period following order for relief); 11 U.S.C. § 1146(b) (trustee of individual in Chapter 11). *See also* 11 U.S.C. § 346(f) (trustee shall withhold and pay over taxes according to applicable state or local tax law); 11 U.S.C. §§ 1106(a) and 704(8) (duties of trustee authorized to operate business include filing periodic reports with taxing authorities).

[12] *See* 11 U.S.C. § 346(b)(1) (income of individual's estate may be taxed by state and local authorities only to the estate, and not to such individual); 11 U.S.C. § 346(f) (trustee must pay state and local withholding taxes); 11 U.S.C. §§ 1129(a), 726(a)(1), 507(a)(1), 503(b)(1)(B)(i) (together, prohibiting a plan of reorganization from being confirmed if it would provide for payment of any unsecured claims before administrative expenses (*e.g.*, any tax "incurred by the estate"). The only exception is in the case of an individual under Chapter 13. *See* 11 U.S.C. § 346(d) (state and local income tax on individual in Chapter 13 may be imposed only on debtor, not estate).

administrative expenses generally "include taxes which the trustee incurs in administering the debtor's estate, including taxes on capital gains from sales of property by the trustee and taxes on income earned by the estate during the case." S. Rep. No. 989, 95th Cong., 2d Sess. 66, *reprinted in* 1978 U.S. Code Cong. & Admin. News 5787, 5852.

The court of appeals swept away this entire structure, as well as applicable state law (*see supra* notes 7-8), through the simple expedient of a "contract trustee" immune from the responsibilities imposed on all other fiduciaries acting under the authority of a federal court. The signatory Amici respectfully submit that the structure of the Bankruptcy Code does not permit such an extraordinary result; instead—consistent with § 960—it requires the trustee (whether appointed before, upon or after confirmation) to pay the state and local taxes incurred as a result of the liquidation process.

IV. The "Contract Trustee" Device Sanctioned By the Court of Appeals Frustrates Congress' Intent to Facilitate State and Local Tax Collection

Section 960 and the structure of the Bankruptcy Code express Congress' intent that fiduciaries acting under the authority of a federal court assume responsibility for reporting and paying state and local taxes. The "contract trustee" device sustained by the court of appeals could seriously undermine compliance with applicable state and local tax laws.

Nearly all the States impose income, sales or use taxes applicable to bankruptcy liquidation activities. *See supra* note 8. Where, as here, capital gains result from liquidating sales, state income taxes applicable to the liquidation process will likely be due.

The court of appeals' decision ignores the practical realities of the situation. Like the federal system, state and local tax systems rely upon *voluntary* reporting and payment. When the trustee pays state taxes in the ordinary course and files state tax returns, bankruptcy does not interfere with the collection of state taxes incurred after the bankruptcy proceeding commences. Here, however, the trustee has taken the position that he is not responsible to file returns or pay these state taxes, based upon his supposedly unique status as a "contract trustee" of a trust created pursuant to a confirmed Chapter 11 plan of reorganization. Such an exemption would utterly frustrate Congress' intent to protect and facilitate the collection of state and local taxes applicable to the liquidation process.[13]

The court of appeals' decision imposes an undue administrative burden on state and local governments to monitor and enforce trustees' compliance with state and local tax laws on a nationwide basis. Many corporations and individuals conduct business in multiple jurisdictions. As businesses have become more interstate in character, with myriad activities nationwide, multistate taxpayers—both individual and corporate—are increasingly common. As a result, many bankruptcy cases result in tax liabilities to numerous States and localities. These States and localities are unlikely to be listed on the debtor's schedule of liabilities or to have any notice of a

[13] When Congress intends to exempt transactions arising out of bankruptcy from state and local taxes, it makes that intent explicit. *See* 11 U.S.C. § 1146(c) (stamp tax or similar tax shall not apply to transfers under a confirmed reorganization plan). *See also Sierra Summit*, 490 U.S. at 851-53 (congressional intent to create exemption from state taxation must be clearly expressed).

potential threat to their revenues. That is particularly true when, as here, taxes are incurred *after* the plan has been confirmed and the trustee refuses even to file a return.[14]

State and local governments cannot realistically be expected to track every bankruptcy case in every federal district in the nation to watch for the establishment of liquidating trusts and the confirmation of reorganization plans that fail to provide for payment of state and local taxes incurred after confirmation. State and local government attorneys, moreover, often encounter significant procedural obstacles to their participation in out-of-state bankruptcies in the form of local counsel requirements.[15]

[14] As noted, the bulk of the unpaid state tax liability in this case arises from the post-confirmation sale of the Miami Center property during the fiscal year ending July 31, 1986, for which no state tax return was filed.

[15] *See, e.g.*, U.S. Bankr. Ct. D. Alaska R. 1(B)(1); U.S. Bankr. Ct. E. & W.D. Ark. R. 2(d); U.S. Bankr. Ct. C.D. Cal. R. 102(2)(c); U.S. Bankr. Ct. D. Colo. R. 16; U.S. Bankr. Ct. S.D. Fla. R. 7 (incorporating U.S. Dist. Ct. S.D. Fla. R. 4); U.S. Bankr. Ct. M.D. Fla. R. 109(c)(1); U.S. Bankr. Ct. D. Del. Order No. 1(c) (incorporating U.S. Dist. Ct. D. Del. R. 8.1); U.S. Bankr. Ct. D. Haw. R. 720(4); U.S. Bankr. Ct. D. Idaho R. 106(d); U.S. Bankr. Ct. M.D. La. R. 104(c)-(e); U.S. Bankr. Ct. D. Md. R. 4(a); U.S. Bankr. Ct. D. Minn. R. 143(b) (local counsel required to file complaint and represent plaintiff in adversary proceeding); U.S. Bankr. Ct. D. N.M. R. 1-102(b); U.S. Bankr. Ct. D. Mont. R. 2 (adopting U.S. Dist. Ct. D. Mont. R. 110-2(c)); U.S. Bankr. Ct. S.D. N.Y. R. 4(a) (local address for service of papers required unless court orders otherwise); U.S. Bankr. Ct. W.D. N.C. Local Form 110-1 (court may approve representation without local

(Continued on following page)

The sheer enormity of the task of monitoring bankruptcy proceedings on a nationwide basis would be staggering. Calculating the taxes due without a return disclosing the debtor's property holdings and business activities would further complicate the task. State and local taxes on multistate business enterprises operating in more than one jurisdiction must be fairly apportioned to satisfy federal Due Process and Commerce Clause requirements. *See Trinova Corp. v. Michigan Dep't of Treasury,* 111 S. Ct. 818, 828 (1991) ("*Trinova*"). Forty-four States and the District of Columbia currently utilize apportionment formulas reflecting a business' in-state and out-of-state property, payroll and sales.[16] Returns disclosing the taxpayer's multistate business activities and property holdings, therefore, are a practical necessity.

(Continued from previous page)

counsel); U.S. Bankr. Ct. S.D. Ohio R. 4.1 (local "case attorney" generally required); U.S. Bankr. Ct. E.D. Tenn. R. 1 (local counsel required for party in adversary proceeding); U.S. Bankr. Ct. D. Utah R. 1(c); U.S. Bankr. Ct. E.D. Va. R. 105(E)(2).

To explore these and other impediments to effective participation in out-of-state bankruptcy proceedings, the National Association of Attorneys General in March 1991 announced the creation of a Bankruptcy Information Exchange Network consisting of attorneys in thirty-six State Attorneys General Offices and the Republic of Guam working in the bankruptcy area. This group's efforts are still in a formative stage.

[16] *See generally Trinova,* 111 S. Ct. at 833; *Container Corp. of America v. Franchise Tax Bd.,* 463 U.S. 159, 170 (1983); J. Hellerstein, *State Taxation: I Corporate Income & Franchise Taxes,* ¶9.6, at 495 (1983).

Section 960 of the Judicial Code reflects Congress' choice that all bankruptcy trustees, including this one, must assume the obligation of voluntarily complying with applicable state and local tax laws. The court of appeals' contrary decision improperly shifts to States and localities the burden of policing trustees' compliance with these laws. Under 28 U.S.C. § 960, it is the trustee's obligation voluntarily to comply with the law.

CONCLUSION

At a time when state and local governments are struggling with fiscal crises, it is critical that their ability to collect taxes be preserved. The court of appeals' decision erroneously creates a heretofore unknown exception from federal and state filing requirements for a so-called "contract trustee." This significant tax loophole threatens to impair States' and local governments' ability to collect revenues to which they are lawfully entitled. The power to tax, an essential attribute of state sovereignty vital to States' ability to function effectively as part of our federal system, and jealously guarded by Congress and this Court, is at stake. Section 960 of the Judicial Code through which Congress intended to protect States' sovereign power of taxation requires reversal of the court of appeals' decision.

Respectfully submitted,

MARY SUE TERRY
Attorney General of Virginia

H. LANE KNEEDLER
Chief Deputy Attorney General

K. Marshall Cook
Deputy Attorney General

Barbara M. Rose
Senior Assistant Attorney General

Martha B. Brissette*
John Patrick Griffin
Assistant Attorneys General

Office of the Attorney General
101 N. Eighth Street
Richmond, Virginia 23219
(804) 786-0061

**Counsel of Record for Amici Curiae*

JULY 1991

Daniel E. Lungren
Attorney General of California

Richard Blumenthal
Attorney General of Connecticut

Charles M. Oberly, III
Attorney General of Delaware

John Payton
Corporation Counsel for the District of Columbia

Robert A. Butterworth
Attorney General of Florida

Michael J. Bowers
Attorney General of Georgia

Warren Price, III
Attorney General of Hawaii

Roland W. Burris
Attorney General of Illinois

Linley E. Pearson
Attorney General of Indiana

Bonnie J. Campbell
Attorney General of Iowa

Robert T. Stephan
Attorney General of Kansas

William J. Guste, Jr.
Attorney General of Louisiana

Michael E. Carpenter
Attorney General of Maine

J. Joseph Curran, Jr.
Attorney General of Maryland

Scott Harshbarger
Attorney General of Massachusetts

Frank J. Kelley
Attorney General of Michigan

Herbert H. Humphrey, III
Attorney General of Minnesota

Michael C. Moore
Attorney General of Mississippi

William L. Webster
Attorney General of Missouri

Marc Racicot
Attorney General of Montana

Robert J. Del Tufo
Attorney General of New Jersey

Tom Udall
Attorney General of New Mexico

Robert Abrams
Attorney General of New York State

Nicholas J. Spaeth
Attorney General of North Dakota

Dave Frohnmayer
Attorney General of Oregon

Ernest D. Preate, Jr.
Attorney General of Pennsylvania

James E. O'Neil
Attorney General of Rhode Island

T. Travis Medlock
Attorney General of South Carolina

Charles W. Burson
Attorney General and Reporter of Tennessee

Dan Morales
Attorney General of Texas

R. Paul Van Dam
Attorney General of Utah

Mario J. Palumbo
Attorney General of West Virginia

Victor A. Kovner
Corporation Counsel for the City of New York